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TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1938 / 9

No. ~~854~~ 30

THE UNITED STATES OF AMERICA, PETITIONER

vs.

THE GLENN L. MARTIN COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR CERTIORARI FILED APRIL 8, 1939

CERTIORARI GRANTED MAY 1, 1939

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1938

No. 854

THE UNITED STATES OF AMERICA, PETITIONER

vs.

THE GLENN L. MARTIN COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

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1 [Caption omitted.]

2 IN DISTRICT COURT OF THE UNITED STATES FOR THE DISTRICT OF MARYLAND

At Law. No. 6239

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, PLAINTIFF

vs.

THE UNITED STATES OF AMERICA, DEFENDANT

Amended petition

Filed December 14, 1937

The petition of The Glenn L. Martin Company, plaintiff, respectively shows and alleges:

1. The plaintiff, The Glenn L. Martin Company, is a corporation duly organized and existing under and pursuant to the laws of the State of Maryland, with its principal place of business at Middle River, Baltimore County, Maryland.

2. This is an action for breach of a contract, entered into between plaintiff and defendant, by the defendant, the action being filed for the recovery of the sum of $7,737.32, exclusive of interest and costs, representing amounts paid by plaintiff applicable directly upon the production of certain supplies called for under the terms of the said contract, the defendant having refused, in violation of the terms of the said contract, to repay to plaintiff the said sum of $7,737.32 or any part thereof. This Court has jurisdiction of the controversy under Sub-division 20 of Section 41 of Title 28 of the United States Code, the amount involved, exclusive of interest and costs, being $7,737.32.

3. On or about June 28, 1934, plaintiff and defendant entered into a contract (U. S. Army Contract No. W535 ac-6861) under which plaintiff agreed to supply to defendant and defendant agreed to purchase and accept from plaintiff certain aircraft and aircraft materials. Article 17 of the said contract provided in part that:

"(3) It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any
3 Federal Tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies

herein contracted for then the prices herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items."

4. During the years 1936 and 1937 plaintiff made certain expenditures for labor in connection with the performance of the said contract, which expenditures were applicable directly upon the production of the supplies called for by the said contract. Of the said expenditures the sum of $769,219.30 represented wages subject to the taxes imposed upon the plaintiff by Titles VIII and IX of the Social Security Act (Act of August 14, 1935, c. 531, 49 Stat. 620, 42 U. S. C. c. 7 (Supp)).

5. Federal Social Security taxes were imposed upon plaintiff by the said Act of August 14, 1935, on the said wages paid in the amount of $769,219.30 as follows:

Year	Wages	Title IX	Title VIII	Total
1936	$766,962.82	$7,669.63		$7,669.63
1937	2,256.48	45.13	$22.56	67.69
Totals	769,219.30	7,714.76	22.56	7,737.32

6. The sum of $7,737.32 has been paid by the plaintiff as Federal and State of Maryland Unemployment Insurance taxes and as Federal Old Age Benefit taxes in accordance with all due requirements of law, and in the amounts set out in paragraph 5 hereof.

7. No portion of the said sum of $7,737.32, paid as aforesaid, has been or will be deducted by the plaintiff from any wages or compensation for services paid to or for the account of any employee of the plaintiff or any other person or persons performing services for it.

4 8. By communication dated October 14, 1937, addressed to Lieut. Col. William F. Volandt, Wright Field, Dayton, Ohio (the person authorized under the terms of said contract to receive such communications), a copy of which is annexed hereto, marked Exhibit A, and prayed to be made a part hereof, the plaintiff requested the defendant to advise it of the manner in which the defendant should be billed for the aforesaid Social Security taxes paid by the plaintiff in the performance of *of* the said contract.

9. By communication dated October 18, 1937, and addressed to the plaintiff, a copy of which is annexed hereto, marked Exhibit B. and prayed to be made a part hereof, the defendant advised plaintiff that the claim of the plaintiff if made would not receive favorable consideration.

10. By communication dated October 25, 1937, addressed to the plaintiff, a copy of which is annexed hereto, marked Exhibit C, and

prayed to be made a part hereof, the defendant reaffirmed the position taken by it in its communication dated October 18, 1937.

11. By communication dated November 10, 1937, addressed to "The Finance Officer, Wright Field, Dayton, Ohio," the person authorized under the terms of the said contract to make payments on behalf of the defendant in accordance therewith, a copy of which is annexed hereto, marked Exhibit D, and prayed to be made a part hereof, the plaintiff forwarded its invoice to the defendant and requested payment in the amount of $7,737.32, representing said Social Security taxes paid on expenditures for labor made during the years 1936 and 1937 in the performance of the above contract. Said invoice is annexed hereto, marked Exhibit E, and prayed to be made a part hereof.

12. By communication dated November 24, 1937, addressed to the plaintiff, a copy of which is annexed hereto, marked Exhibit F, and prayed to be made a part hereof, the defendant, by the person authorized under the terms of the said contract to make payments in accordance therewith, refused to pay the said claim for Social Security taxes paid during the years 1936 and 1937 on the said contract, and returned the said invoice for cancellation.

5 13. All of the steps taken by the plaintiff to secure the repayment of the said taxes of $7,737.32, paid as aforesaid, were taken in accordance with the terms and requirements of the said contract between the plaintiff and the defendant.

Wherefore the plaintiff demands judgment against the defendant in the sum of $7,737.32 with interest thereon as provided by law, for costs and for such other and further relief as may be proper.

SEMMES, BOWEN & SEMMES,
JOHN T. KOEHLER,
Counsel for Plaintiff,

2500 Baltimore Trust Building, Baltimore, Maryland.

[*Duly sworn to by M. G. Shook; jurat omitted in printing.*]

In United States District Court

Defendant's plea to amended petition

Filed March 14, 1938

The defendant, United States of America, by Bernard J. Flynn, United States Attorney for the District of Maryland, for pleas to the amended petition filed herein, and each and every count thereof, says:

1. That it never promised as alleged.
2. That it was never indebted as alleged.

BERNARD J. FLYNN,
United States Attorney.

6 In United States District Court

Docket entry

March 14, 1938—Issues joined.

In United States District Court

Verdict

May 7, 1938. Verdict for the Defendant.

In United States District Court

Judgment

May 10, 1938. Judgment on verdict absolute in favor of the defendant for costs.

In District Court of the United States for the District of Maryland

At Law. No. 6239

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, PLAINTIFF

vs.

UNITED STATES OF AMERICA, DEFENDANT

Bill of exceptions

Filed June 14, 1938

Be it remembered, that at the trial of this cause in the March Term, 1938, of this Court, the Honorable W. Calvin Chestnut presiding, the following proceedings were had, to wit:

Stipulation as to certain facts

It was stipulated and agreed by and between counsel for the Plaintiff and the Defendant that on June 28, 1934, the Plaintiff and the Defendant entered into a contract (United States Army Contract No. W535-ac 6861—"Standard Form No. 32—approved by the President June 10, 1927"), under which contract the Plaintiff agreed to supply to the Defendant, and the Defendant agreed to purchase from the Plaintiff, certain aircraft and aircraft materials; that following the passage of the Federal Social Security Act and during the years 1936 and 1937, the Plaintiff made certain expenditures as

7 wages for labor in connection with the performance of the said contract, on which wages Federal Social Security taxes were imposed; that by virtue of the provisions of Arti-

cle 17 (3) of the said contract (which Article is set out in full on page 14 of this Record and made a part hereof by the Court below), the Plaintiff claimed that it was entitled to recover from the Defendant all amounts paid by it as Federal or State of Maryland Social Security taxes on expenditures for labor made by the Plaintiff in the performance of the said contract; that, in furtherance of such claim, the letters attached to the petition of the Plaintiff were written and the replies set out and similarly attached to said petition received and that all of such letters were correct copies of the original letters so written and received.

Thereupon, the Plaintiff introduced in evidence its copy of the contract between it and the Defendant, with leave to substitute a photostatic copy thereof at the conclusion of the hearing. The contract so introduced was marked "Plaintiff's Exhibit No. 1."

Thereupon, Morgan R. Schermerhorn, a witness of lawful age, after being first duly sworn, was examined and testified as follows:

That he is and has been employed by the Plaintiff since April 1931, and that he is and has been since January 1937, the Assistant Treasurer of the Plaintiff; that he now has and did have charge of the books of the Plaintiff during the period in which the said contract was being performed; that during the years 1936 and 1937, the Plaintiff paid wages of $766,962.82 and $2,256.48, respectively, for labor charged to the performance of the said contract; that Social Security taxes were imposed on the wages so paid and were paid by the Plaintiff as follows: $7,669.63 (1% of $766,962.82) for the year 1936, of which amount $6,902.67 was paid to the State of Maryland under its Unemployment Compensation Act, and $766.96 was paid to the Commissioner of Internal Revenue—Baltimore, Maryland, under the Title IX of the Federal Act, and $67.69 (3% of $2,256.48) for the year 1937, of which amount $40.62 was paid to the State of Maryland under its Unemployment Compensation Act, and $4.51 and $22.56, respectively, was paid to the Collector of Internal Revenue—Baltimore, Maryland, under Titles IX and VIII of the Federal Act.

8 That the Plaintiff, in determining the costs allocable to each contract in process of completion in its plant follows the following accounting procedure; namely, a record is maintained of all direct labor costs on each contract and such direct labor costs are charged monthly to such contract. All costs other than direct labor (which includes all mechanical labor in the factory, such as tool and engineering labor) are charged to overhead on a monthly basis and each contract bears its share of overhead charges on a percentage basis, that percentage being the quotient of the total overhead for the particular month divided by the total direct labor costs for such month. For example, if the total direct labor costs and the total overhead costs of one month for all contracts amounted to $100,000.00 and $50,000.00, respectively, the monthly overhead charges allocable to each contract would be 50% of the direct labor costs

charged to such contract. If four contracts were in process of completion at the same time, the direct labor and overhead costs of all contracts being $100,000.00 and $50,000.00, respectively, overhead costs would be allocated in the following manner:

Contract	Direct labor costs	Percentage	Overhead costs
A	$40,000.00	50%	$20,000.00
B	30,000.00	50%	15,000.00
C	20,000.00	50%	10,000.00
D	10,000.00	50%	5,000.00
Totals	100,000.00		50,000.00

That the above accounting practice was followed in determining the direct and overhead labor costs under the contract here involved, and that he, the said Morgan R. Schermerhorn, prepared a detailed break-down of the labor costs of $766,962.82 and $2,256.48, allocable to the said contract for the years 1936 and 1937, respectively, from the books of the Plaintiff; that such break-down, introduced in evidence as "Plaintiff's Exhibit No. 2," reveals the following in summarized form:

9 THE GLENN L. MARTIN COMPANY

Total labor charged to Army Contract No. W535 ac—6861 from January, 1936, to May, 1937, inclusive

Item No.		1936	1937
1	Direct labor	$544,679.95	$1,560.82
2	Tool labor	5,430.68	2.80
3	engineering labor	6,757.12	18.23
4	Overhead labor (direct and tool)	200,549.99	672.35
5	Overhead labor (engineering)	9,545.08	4.28
6	Total labor costs	766,962.82	2,256.48

That Item 4 (Overhead labor—direct and tool) was determined as follows: (a) the percentage of overhead allocable to each contract for the particular month was determined, as set forth above, by dividing the total direct labor costs (direct, tool, and engineering labor) into the total factory overhead costs (exclusive of engineering overhead) for such month; (b) the total labor costs included in such factory overhead were then determined; and (c) the percentage determined in (a) was applied against the total labor included in factory overhead for such month and the result was the direct and tool overhead labor allocable to the particular contract for such month. Item 4 represents the yearly total of the amounts so determined for each month.

That Item 5 (Overhead labor—engineering) was determined in the same manner by applying the percentage which the engineering over-

head applicable to the particular contract bore to the total engineering overhead for all contracts against all tool labor included in engineering overhead.

That all taxes, including Federal and State of Maryland Social Security taxes, paid by the plaintiff, except Federal and State income taxes, were included by the Plaintiff in overhead.

That the methods of accounting employed by the Plaintiff conformed to a standard code of accounting approved by the War Department of the Defendant; that a daily audit was made by the Defendant of the accounts of the Plaintiff during the performance of the said contract, and that a final audit thereof was similarly made when the contract was completed.

The above represents a summary of all the evidence in the case and, following oral argument by counsel, the Plaintiff moved for a judgment in its favor and then and there filed a motion in writing on the grounds therein stated, and the same was made a part of the Record, the said motion being as follows:

Motion for judgment

Comes now the plaintiff in the above entitled cause and moves the Court that judgment in said action be entered in favor of the plaintiff and against the defendant for the sum of seven thousand seven hundred thirty-seven dollars and thirty-two cents ($7,737.32) with interest thereon as provided by law.

SEMMES, BOWEN & SEMMES,
JOHN T. KOEHLER,
Attorneys for Plaintiff.

The following prayers were submitted by the Plaintiff and the Court ruled on each of said prayers, in accordance with the views stated by it in its opinion, and noted exceptions for the Plaintiff as to adverse rulings:

Plaintiff's first prayer

The plaintiff prays the Court to rule as a matter of law that the evidence in this case is legally sufficient to entitle the plaintiff to recover and that, therefore, the verdict of the Court should be for the plaintiff. (Refused.)

Plaintiff's second prayer

The plaintiff prays the Court to rule as a matter of law that the amounts paid by the plaintiff as Federal and State social security taxes on labor engaged in the performance of the contract involved in this case were taxes applicable directly on the production, manufacture or sale of the supplies called for by the contract. (Refused.)

11 *Plaintiff's third prayer*

The plaintiff prays the Court to rule as a matter of law that the amounts paid by the plaintiff as Federal and State social security taxes on labor engaged in the performance of the contract in this case were taxes which were properly includable in plaintiff's cost of production of the supplies called for by the contract. (Refused—because, while academically correct, it is not of controlling importance in this case.)

Plaintiff's fourth prayer

The plaintiff prays the Court to rule as a matter of law that the requirements of the sentence appearing in Article 17 (3) of the contract between the plaintiff and defendant, namely:

"If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein contracted for, then the prices herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items" have been satisfied if such taxes were imposed by Congress after the contract was signed, were paid by the plaintiff and increased the cost of production of the supplies called for by the contract. (Refused—see Opinion.)

Plaintiff's fifth prayer

The plaintiff prays the Court to rule as a matter of law that if the sentence appearing in Article 17 (3) of the contract between the plaintiff and defendant—

"If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein con-
12 tracted for, then the prices herein stipulated will be increased or deceased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items" is interpreted literally, no sales tax or processing tax could be recovered because such taxes are not imposed on the articles sold or processed but are imposed upon the sale or processing of such articles. (Granted—But see Opinion.)

Plaintiff's sixth prayer

The plaintiff prays the Court to rule as a matter of law that the intent of the parties to the contract was to increase the stipulated

prices by an amount equal to new taxes or charges imposed by Congress after the contract was signed which increased the cost of production and to decease the stipulated prices by an amount equal to any decrease in the cost of production occasioned by changes in rates, made by Congress after the contract was signed, of taxes which were in effect when the contract was signed. (Refused—See Opinion.)

Plaintiff's seventh prayer

The plaintiff prays the Court to rule as a matter of law that whether social security taxes are, for accounting purposes, treated as items of cost or as items of overhead, the cost of production in either case should be increased by the amounts of such taxes paid with respect to labor engaged in the production of the supplies produced, manufactured, or sold. (Refused as academic—See Opinion.)

Plaintiff's eighth prayer

The plaintiff prays the Court to rule as a matter of law that the total amount of the social security taxes paid to the United States and to the State of Maryland during the year 1936 and 1937 with respect to wages paid to labor engaged in the performance of the contract, was imposed by Congress under Titles VIII and IX of the Federal Social Security Act. (It is unnecessary to rule on this proposition—See the Opinion.)

13 *Ruling on plaintiff's request for findings of fact and conclusions of law*

The Plaintiff filed a written request for findings of fact and conclusions of law, but the requested findings were refused by the Court, the reason for such refusal being noted on such request for findings in the following language:

"Request refused because facts found have been stated in the opinion in the case and conclusions of law requested are rejected as unsound or immaterial."

Following due consideration, the Court made an entered its opinion, directing the verdict to be entered in favor of the Defendant and denying the Plaintiff's motion for judgment in the following language:

"Motion overruled—see opinion in the case."

In such opinion, the Court allowed the Plaintiff timely and separate exceptions to the granting of the Defendant's motion for judgment, to the denial of the Plaintiff's motion for judgment, and to the refusal of the Plaintiff's first, second, third, fourth, sixth and seventh prayers, and to the refusal of the Court to grant or refuse the Plaintiff's eighth prayer. The judgment of the Court was entered on May 10th, 1938.

And now, in furtherance of justice and that right may be done, the Plaintiff tenders and presents the foregoing as the Bill of Exceptions

in the appeal from the action of the Court in the foregoing case, and prays that the same may be settled, allowed, signed, and sealed by the Court and made a part of the Record to be transmitted to the United States Circuit Court of Appeals for the Fourth Circuit.

SEMMES, BOWEN & SEMMES,
JOHN T. KOEHLER,
Attorneys for Plaintiff.

Order settling bill of exceptions

The foregoing Bill of Exceptions duly allowed, settled, signed, and sealed, this 11th day of June, 1938.

W. CALVIN CHESNUT,
United States District Judge.

No objection as to form:
BERNARD J. FLYNN,
U. S. Attorney.
G. RANDOLPH AIKEN,
Asst. U. S. Attorney,
Attorneys for Defendant.

14 In District Court of the United States for the District of Maryland

At Law. No. 6239

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, PLAINTIFF

vs.

UNITED STATES OF AMERICA, DEFENDANT

Opinion

Filed May 7, 1938

CHESNUT, District Judge.

This is an action at law against the United States under the Tucker Act (28 U. S. C. A., s. 41 (20)). Such a suit is of course tried without a jury. The plaintiff, The Glenn L. Martin Company, a Maryland corporation with its principal place of business in Baltimore County, Maryland, is suing the Government to recover $7,737.32 (with interest) which is alleged to be due as extra compensation under its contract with the Government dated June 28, 1934, for the sale and delivery of certain aircraft and aircraft materials. In Article 17 (3) of the contract there was the following provision:

"(3) It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any Federal Tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge and other taxes or charges are

imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein, and are paid by the contractor on the articles or supplies herein contracted for, then the price herein stipulated will be increased or decreased accordingly and any amount due the contractor as the result of such change will be charged to the Government and entered on vouchers as separate items."

The plaintiff claims the extra compensation under the second
15 sentence of this provision, by virtue of the incidence of taxes paid by it under the Act of Congress known as the Social Security Act of August 14, 1935, ch. 531, 49 Stat. 620; 42 U. S. C. A. (Supp. ch. 7). This Act was passed and became effective after the making of the contract. Under the Act and during the performance of the contract by the plaintiff, the latter paid in wages to employees allocated to work in the performance of the contract, $766,962.82 in the year 1936, and $2,256.58 in the year 1937. Under Title IX of the Act the plaintiff paid taxes (at the rate of 1%) on wages for the year 1936, $7,669.63 and for the year 1937, $45.13, and in the latter year also paid $22.56 taxes under Title VIII of the Act. The total taxes so paid by the plaintiff on wages of employees, during the performance of the contract, for the two years amounted to $7,737.32. Of the total amount so paid $7,714.76 was paid for unemployment insurance under Title IX of the Act, 10% thereof being paid to the federal government and 90% (if allowed by the Act of Congress) being paid to the State of Maryland under the Maryland Unemployment Compensation Law, Laws of Maryland, Extraordinary Session December 19, 1936, ch. 1. No part thereof will be deducted from wages due to employees, that is to say, the taxes are in addition to the wages paid.

In due course the plaintiff rendered bills to the Government for the amount of the taxes so paid, $7,737.32, but payment has been refused on the ground that it is not due under the wording of the contract. The question presented is whether by the effect of the Social Security Act the taxes so paid were "made applicable *directly* upon production, manufacture, or sale of the supplies called for herein and are paid by the contractor *on* the articles or supplies herein contracted for." [Italics supplied.] It will be noted that the plaintiff contractor must show that the taxes were (1) made applicable directly on production *and* (2) paid on the supplies.

The primary contention advanced by the Government is that the Social Security taxes were not at all imposed upon production, manufacture or sale, or *on the articles* or supplies contracted for because they are *excise taxes on the employer*, for the benefit of having employees, and were described by the Supreme Court in Steward Machine Co. v. Davis, 301 U. S. 548, 578, as follows:

16 "The tax which is described in the statute as an excise is laid with uniformity throughout the United States as a duty, an impost or an excise *upon the relation of employment.*" [Italics supplied.]

See also Helvering v. Davis, 301 U. S. 619. It is urged that the language contemplates a tax on or related to the production, or employment or use of physical property, while the Social Security Tax affects only the relation of employment, and is not associated in any way with tangible property. On the other hand the plaintiff contends that the fair and reasonable construction of the whole of the contract provision entitled it to recover the taxes so paid because they constituted "an increase in cost of production."

The contention of the Government sets up a construction of the wording which seems very narrow and literal. We must remember that we are construing a business contract rather than dealing primarily with a tax case. Batavia Mills, Inc., v. United States, Ct. Claims, June 1, 1937. And in a business or economic sense the taxes paid did result in an increase of the cost of production to the contractor. The general purpose of the clause doubtless was to indemnify the contractor against increased cost of production due to increased taxes imposed by subsequent Acts of Congress, although the scope of the indemnity must be limited by the language used. The construction should be reasonable in the light of the subject matter, rather than narrowly literal. In this view it does not seem of controlling importance whether the tax is classified as a tax or duty, an impost, or excise (Thomas v. United States, 192 U. S. 363, 370), or whether it is, in its purely legalistic concept, imposed on the employer upon the relation of employment, or on the product of the employment. A sales tax is an excise tax on sales rather than on the articles sold; and similarly a process tax is an excise on the act of processing rather than on the product. (See United States v. Butler, 297 U. S. 1, 57, 61.) It would seem fairly clear that such taxes would properly be regarded as within the language of the contract provision although not "paid by the contractor on the articles or supplies herein contracted for," unless excluded by other wording of the contract. See Willcuts v. Bunn, 282 U. S. 216, 228. By
like reasoning it would seem logical to hold that a tax on the
17. employer, measured by his payroll, which undoubtedly increases his production cost, might be regarded as a tax on production. It is, however, unnecessary to expressly so determine in this case, in view of the conclusion now to be stated with respect to the force of the word "directly."

The construction contended for by the plaintiff is too broad in that it ignores the significance of the word "directly" in the contract clause which provides for additional compensation only if the new tax is by the Act of Congress "made applicable directly upon production, manufacture, or sale of the supplies called for herein." The tax here dealt with is described in the taxing Act itself as an excise tax "with respect to having individuals in his employ." U. S. C. A., Title 42, s. 1101, s. 1004. And the Supreme Court has described it as "an excise upon the relation of employment." In other words, it is a tax on the employer measured by his payroll. It seems

quite clear that such a tax is not "applicable directly upon production, manufacture, or sale." It becomes payable irrespective of the product of the employment. In the economic sense it does increase the cost of production but its effect is indirect rather than direct. The nature of the tax is an enforced contribution by the employer for the ultimate benefit of employees generally, and it would seem to be similar in nature to other burdens placed upon an employer by law for the safety or welfare of employees, such as required fire escapes on high buildings, and sanitary regulations for working conditions. All such humanitarian requirements clearly do actually increase manufacturing costs although they operate indirectly through overhead expense rather than directly, as would increased wages paid for the work done. The wording of the contract provision taken as a whole is not susceptible of the broad construction contended for by the plaintiff and clearly is not equivalent to "any increased cost of production" caused by new taxation. New and additional state taxes, whatever their effect upon the cost of production, are clearly not included; and it is equally clear that the provision is not worded in such a way as to cover any and all additional Federal taxes because those that are included are definitely limited to such as are made applicable directly upon production, manufacture, or sale. It is, I think, impossible to escape the significance of the word "di-
18 rectly" in this context, as it is obviously an important word of limitation, of familiar legal use. See Liggett and Myers Co. v. United States, 299 U. S. 383, 386.

The plaintiff submits the argument that the function of the word "directly" in the contract clause is only to limit the generality of the words "other taxes or charges" and thus restrict their application to new taxes or charges "which increase the cost of production of the supplies called for;" thus for instance, excluding income taxes which do not increase the cost of production but simply diminish net profits, if any. But this seems an untenable construction of the phraseology because the new taxes comprehended in the context, whether specifically referred to as "sales taxes, processing taxes, adjustment charges" or in the general terms of "other taxes or charges" must all be "made applicable directly upon production, manufacture, or sale" in order to constitute the basis for additional compensation.

Counsel inform me that the contract provision here under consideration has appeared in many War Department contracts during a period of several years past, but that they have been unable to ascertain how the clause has heretofore been applied in actual practice, as a possible aid to construction. Reference has been made to the case of Batavia Mills, Inc. v. United States, decided June 1, 1937, by the Court of Claims. But that case is not in point here. The relevant provision in the contract there, after reference to "all sales taxes, duties, imposts, revenues, excise or other taxes applicable to the supplies" then in force was "if any new taxes are made applicable to such supplies by Congress after the date of opening of the

bid upon which this contract was based." then the price should be increased. The contractor with the Government in that case, in performance of its contract, had been obliged to pay an increased cost to its vendor by reason of processing taxes paid by the latter to the United States under the Agricultural Adjustment Act of May 12, 1933, as amended. The Court of Claims rendered judgment for the plaintiff contractor for the amount in dispute, but it will be noted from the opinion in the case that the Government's denial of liability was put "on the ground that said amount was not paid by the
19 plaintiff directly to the United States." And it will be noted that the contract provisions did not require as a condition for the additional compensation that the new taxes should be "made directly applicable to such supplies."

I conclude, therefore, that the verdict in this case must be for the defendant and the Clerk of the Court is instructed to so enter it to be followed in due course for judgment for the defendant with costs.

Both parties have requested the granting of certain submitted prayers on rulings of law, and I have ruled on them respectively in accordance with the view stated in this opinion and have filed them with the Clerk of the Court. Exceptions are noted for the plaintiff as to adverse rulings.

W. CALVIN CHESTNUT,
U. S. District Judge.

Dated May 7, 1938.

In United States District Court

Assignment of errors

Filed June 27, 1938

Comes now the Plaintiff, by its attorneys, Semmes, Bowen & Semmes and John T. Koehler, and makes and files the following Assignment of Errors upon which the Plaintiff will rely for the prosecution of its appeal from the judgment of this Court made and entered in the office of the Clerk of the District Court of the United States, for the District of Maryland, on May 10th, 1938:

1. The District Court erred in overruling the Plaintiff's motion for judgment for Seven thousand, seven hundred and thirty-seven dollars and thirty-two cents ($7,737.32), with interest.

2. The District Court erred in failing and refusing to enter judgment in favor of the Plaintiff.

3. The District Court erred in granting the Defendant's motion for judgment and in entering judgment in favor of the Defendant.

20 4. The District Court erred in refusing "Plaintiff's First Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the evidence in this case is legally sufficient to entitle the plaintiff to re-

cover and that, therefore, the verdict of the Court should be for the plaintiff."

5. The District Court erred in refusing "Plaintiff's Second Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the amounts paid by the plaintiff as Federal and State social security taxes on labor engaged in the performance of the contract involved in this case were taxes applicable directly on the production, manufacture, or sale of the supplies called for by the contract."

6. The District Court erred in refusing "Plaintiff's Third Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the amounts paid by the plaintiff as Federal and State social security taxes on labor engaged in the performance of the contract in this case were taxes which were properly includable in plaintiff's cost of production of the supplies called for by the contract."

7. The District Court erred in refusing "Plaintiff's Fourth Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the requirements of the sentence appearing in Article 17 (3) of the contract between the plaintiff and defendant, namely:

"'If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein contracted for, then the prices herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items' have been satisfied if such taxes were im-
91 posed by Congress after the contract was signed, were paid by the plaintiff and increased the cost of production of the supplies called for by the contract."

8. The District Court erred in refusing "Plaintiff's Sixth Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the intent of the parties to the contract was to increase the stipulated prices by an amount equal to new taxes or charges imposed by Congress after the contract was signed which increased the cost of production and to decrease the stipulated prices by an amount equal to any decrease in the cost of production occasioned by changes in rates, made by Congress after the contract was signed, of taxes which were in effect when the contract was signed."

9. The District Court erred in refusing "Plaintiff's Seventh Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that whether social security taxes are, for accounting purposes, treated as items of cost or as items of overhead, the cost of production in

either case should be increased by the amounts of such taxes paid with respect to labor engaged in the production of the supplies produced, manufactured, or sold."

10. The District Court erred in refusing to grant or refuse "Plaintiff's Eighth Prayer," reading as follows:

"The plaintiff prays the Court to rule as a matter of law that the total amount of the social security taxes paid to the United States and to the State of Maryland during the year 1936 and 1937 with respect to wages paid to labor engaged in the performance of the contract, was imposed by Congress under Titles VIII and IX of the Federal Social Security Act."

11. The District Court erred in concluding as a matter of law that no portion of the amounts paid by the Plaintiff as Federal and State Social Security taxes on labor engaged in the performance of the contract involved in this case was, within the meaning of Article 17 (3) of the contract, taxes applicable directly on the
22 production, manufacture, or sale of the supplies called for by such contract.

12. The District Court erred in concluding as a matter of law that the amounts paid by the Plaintiff as Federal and State Social Security taxes on direct labor engaged in the performance of the contract involved in this case were not, within the language of Article 17 (3) of such contract, taxes applicable directly on the production, manufacture, or sale of the supplies called for thereby.

13. The District Court erred in concluding as a matter of law that the amounts paid by the Plaintiff as Federal and State Social Security taxes on overhead labor engaged in the performance of the contract involved in this case were not, within the language of Article 17 (3) of such contract, taxes applicable directly on the production, manufacture, or sale of the supplies called for thereby.

Wherefore, the Plaintiff prays that the judgment of the District Court for the District of Maryland be reversed, and that the said District Court be directed to enter judgment for the Plaintiff in the amount of Seven thousand, seven hundred and thirty-seven dollars and Thirty-two cents ($7,737.32), with interest thereon, and for such other and further relief as to the Court may seem just.

SEMMES, BOWEN & SEMMES,
JOHN T. KOEHLER,
Attorneys for Plaintiff.

In United States District Court

Stipulation as to exhibits attached to and forming a part of amended petition

Filed June 28, 1938

It is hereby stipulated and agreed, by and between the par-
23 ties to the above cause, in order to obviate the necessity for

including in the Record on Appeal the exhibits attached to and made a part of the amended Petition.

1. That the allegations of fact set out in Paragraphs 8, 9, 10, 11, and 12, with respect to the matters contained in Exhibits A, B, C, D, E, and F, are correct and set forth in substance the statements contained in such exhibits.

JOHN T. KOEHLER,
Attorney for Plaintiff.
BERNARD J. FLYNN,
United States Attorney,
Attorney for Defendant.

In United States District Court

Stipulation of counsel as to record on appeal

Filed June 28, 1938

It is stipulated and agreed by and between the parties to the above cause that the transcript of record for the appeal shall consist of the following:

1. Plaintiff's amended petition, omitting the attached exhibits,
2. Defendant's pleas to amended petition,
3. Stipulation as to exhibits attached to and forming a part of amended petition,
4. Docket entry of joinder of issue,
5. Verdict and judgment,
6. Bill of Exceptions,
7. Assignment of Errors,
8. Docket entries,
9. Stipulation as to record on appeal,
10. Opinion of Judge W. Calvin Chesnut,
24 11. Memorandum of the Clerk,
12. Order to transmit Record,
13. Clerk's Certificate.

JOHN T. KOEHLER,
Attorney for Plaintiff.
BERNARD J. FLYNN,
United States Attorney,
Attorney for Defendant.

In United States District Court

[Title omitted.]

Docket entries

1937

Decr. 14—Petition under Title 28, Sec. 41, Sub-division 20, U. S. Code, for breach of contract, filed. (Service admitted by U. S. Atty.)

Decr. 14—Affidavit of service of copy of petition on U. S. Atty. and of mailing copy to U. S. Attorney General, filed.

1938

Feby. 12—Petition of U. S. Attorney and Order of Court extending the time for filing pleas herein for thirty days from 12 February, 1938, filed.

Mch. 14—Pleas 1 & 2 filed. Issues joined.

Apr. 20—Case tried before Court (Chesnut, J.).

Apr. 20—Plaintiff's (8) and Defendant's (2) Prayers filed.

25 Apr. 20—Plaintiff's request for Findings of Fact and Conclusions of Law, filed.

Apr. 20—Pltff's motion for judgment filed.

May 7—Verdict for the Defendant, Opinion of Court, filed.

May 7—Judgment on Verdict nisi.

May 10—Judgment on Verdict absolute in favor of the Defendant for costs.

June 14—Plaintiff's Bill of Exceptions, filed.

June 27—Petition of Plaintiff for Allowance of appeal and Order of Court allowing appeal and fixing the penalty of the appeal bond in the sum of $300, filed.

June 27—Assignment of Errors, filed.

June 27—Citation issued retble within forty days. (Service acknowledged.)

June 28—Stipulation of Counsel re exclusion of Exhibits attached to amended Petition from record on appeal filed.

June 28—Stipulation as to Transcript of Record on Appeal filed.

In United States District Court

Memorandum of the clerk

(1) Petition for Appeal filed 27th June, 1938.

(2) Appeal granted 27th June, 1938.

(3) Appeal Bond dated 14th June, 1938. Obligors: The Glenn L. Martin Company, as principal, and Aetna Casualty & Surety Company of Hartford, Connecticut, as Surety. Penalty: $300.00, conditioned for costs.

(4) Citation dated 27th June, 1938. (Service acknowledged.)

26 In United States District Court

Order to transmit record

And, thereupon, it is Ordered by the Court here that a transcript of the record and proceedings of the cause aforesaid, together with all things thereunto relating, be transmitted to the said United

States Circuit Court of Appeals for the Fourth Circuit and the same is transmitted accordingly.

Test:

ARTHUR L. SPAMER,
Clerk, U. S. District Court.

[Clerk's certificate to foregoing transcript omitted in printing.]

27 In United States Circuit Court of Appeals for the Fourth Circuit

No. 4375

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, APPELLANT

vs.

UNITED STATES OF AMERICA, APPELLEE

Appeal from the District Court of the United States for the District of Maryland, at Baltimore

Docket entries

July 16, 1938, the transcript of record is filed and the cause docketed.

Same day, the original petition for appeal, order allowing appeal, bond, and citation are certified up.

Same day, the appearance of John T. Koehler is entered for the appellant.

Same day, twenty-four copies of the printed record are filed.

July 28, 1938, the appearance of Jas. W. Morris, Assistant Attorney General; Sewall Key, Special Assistant to the Attorney
28 General, and Bernard J. Flynn, United States Attorney, is entered for the appellee.

September 17, 1938, stipulation as to the time for the filing of the respective briefs is filed.

29 *Addendum to transcript of record; printed at the instance of appellee*

Filed September 28, 1938

[Caption omitted.]

30 In United States District Court

[Title omitted.]

Supplemental stipulation respecting record

Filed September 16, 1938

Referring to the stipulations respecting the record on appeal which were heretofore filed on June 28, 1938, entitled, respectively, "Stipu-

lation as to Exhibits attached to and Forming a Part of Amended Petition" and "Stipulation of Counsel as to Record on Appeal," which appear at pages 22–24 of the printed transcript of record filed in the United States Circuit Court of Appeals for the Fourth Circuit in connection with the appeal heretofore allowed in this matter, at the request of the defendant, the plaintiff not agreeing that it is necessary to the determination of the issues involved in the appeal, it is now stipulated and agreed by and between the parties to the above cause that the papers attached to and made a part of the plaintiff's amended petition herein and described as Exhibits A, B, C, D, E, and F, respectively, which are referred to in Paragraphs 8, 9, 10, 11, and 12, respectively, of said amended petition, may be printed and transmitted to the Circuit Court of Appeals for the Fourth Circuit as an addendum to the record on appeal under Rule 14 of said Circuit Court of Appeals.

It is further stipulated and agreed that the Exhibit referred to in the Bill of Exceptions as "Plaintiff's Exhibit No. 1" (Transcript of Record on Appeals, page 7), may be transmitted to the Circuit Court of Appeals for the Fourth Circuit for consideration and inspection in connection with the appeal because it is impracticable to
31 have this Exhibit printed in the record or in any addendum thereto.

It is further stipulated and agreed that the Circuit Court of Appeals for the Fourth Circuit shall determine whether the appellant or appellee shall pay the cost of printing the addendum to the record and of forwarding to the said Court Plaintiff's Exhibit No. 1.

SEMMES, BOWEN & SEMMES,
JOHN T. KOEHLER,
Attorneys for Plaintiff.
BERNARD J. FLYNN,
United States Attorney,
Attorney for Defendant.

32 In United States District Court

[Title omitted.]

Order for transmission of original exhibit to the United States Circuit Court of Appeals for the Fourth Circuit under par. 4, rule 14, of that court

Filed September 16, 1938

Whereas, it appears that it is necessary and proper that the original Exhibit, referred to in the Bill of Exceptions heretofore filed in this cause as "Plaintiff's Exhibit No. 1," be available for use and inspection by the United States Circuit Court of Appeals for the Fourth Circuit in connection with appellate proceedings herein; and

Whereas, it further appears that said Exhibit is of such a character that it would be impracticable to have it printed in the record or in an addendum thereto;

Now, therefore, the parties hereto, by their respective counsel, having agreed by stipulation heretofore filed to the transmission of the said original Exhibit to the United States Circuit Court of Appeals for the Fourth Circuit, as provided by Par. 4, Rule 14, of said Court, it is accordingly Ordered, by the District Court of the United States for the District of Maryland, this 16th day of September, 1938, that when the addendum to the record on appeal herein is forwarded by the Clerk of this Court to the United States Circuit Court of Appeals for the Fourth Circuit, that the said Clerk also forward said original Exhibit to the Clerk of the said United States Circuit Court of Appeals, to be kept by the said Clerk for use and inspection by the said United States Circuit Court of Appeals until the determination of the appeal, said Exhibit thereupon to be returned to this Court.

W. CALVIN CHESNUT,
United States District Judge.

33 *Exhibit A attached to amended petition of plaintiff*

OCTOBER 14, 1937.

From: The Glenn L. Martin Company, Baltimore, Maryland.
To: Lieut. Col. William F. Volandt, Wright Field, Dayton, Ohio.
Subject: Contract W 535ac-6861 dated June 28, 1934.
Reference: (a) Paragraph 3 of Article Seventeen of subject Contract.

1. In accordance with Paragraph 3 of Article 17, of the subject Contract, if any Sales Tax, Processing Tax, or other tax or charge is imposed by Congress subsequent to the date of the Contract, and made applicable directly upon the production, manufacture, or sale of the supplies called for in the Contract, and is paid by the Contractor, then the prices in the Contract are to be increased or decreased accordingly, and any amount due the Contractor as a result of such tax is to be charged to the Government as a separate item.

2. The Social Security Law, imposing an Unemployment Insurance Tax on all labor, was passed by Congress subsequent to the date of the subject Contract, and was operating as a tax to the extent of One Percent (1%) of the labor expended on the Contract in 1936. The Contract was completed in the Fall of 1936, and we are now preparing the necessary data for a separate invoice covering the amount of Social Security Tax which we paid on the labor used in prosecuting the Contract.

3. Will you please advise whether any special forms are to be filled out and submitted along with our invoice, and the proper procedure to follow in submitting this item for payment? We presume that the invoice is to be rendered, and will be approved for payment by your office in the usual manner.

Yours very truly,

THE GLENN L. MARTIN COMPANY,
By M. G. SHOOK, *Treasurer.*

34 *Exhibit B attached to amended petition of plaintiff*

In reply refer to EHA:bkh:63.

OCTOBER 18, 1937.

Contract W 535 ac-6861.
The GLENN L. MARTIN COMPANY,
Baltimore, Maryland.

1. Receipt is acknowledged of your letter of October 14, 1937, indicating your attention to file claim under paragraph (3) of Article 17 of subject contract for reimbursement of taxes at the rate of one percent (1%) of the wages paid by you for labor used in the manufacture of airplanes delivered to the Government under subject contract and in connection therewith requesting advice on appropriate procedure involved with particular reference to any special forms employed:

2. You state that the taxes for which reimbursement is to be claimed arise from the Social Security Law:

"Imposing an Unemployment Insurance Tax on all labor, which was passed by Congress subsequent to the date of the subject contract and was operating as a tax to the extent of one percent (1%) of the labor expended in the contract in 1936."

You further state that the subject contract was completed in the fall of 1936.

3. Subject contract provisions herein referred to stipulated:

"It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any Federal Tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge or other taxes or charges
35 are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein contracted for then the prices herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items."

Section 804, of the Act of August 14, 1935 (Social Security Act), provided, in pertinent part, that:

"In addition to other taxes, every employer shall pay an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined in section 811) paid by him after December 31, 1936, with respect to employment (as defined in section 811) after such date:

"(1) With respect to employment during the calendar years 1937, 1938, and 1939, the rate shall be 1 per centum."

4. Inasmuch as subject contract was completed, according to your statement, in the fall of 1936, it would appear that no taxes imposed

by the Act of August 14, 1935, should have been made with respect to employment involved in subject contract, but notwithstanding this fact it is obvious that there is no authority under the contract to make payment for the claim your have in mind. It will be noted that the tax which may be considered as an addition to the contract price is any sales tax, processing tax, adjustment charge, or other taxes imposed by or changed by the Congress subsequent to the date of the contract and made applicable directly upon production, manufacture, or sale of the supplies called for in the contract. The tax imposed by Section 804 of the Act of August 14, 1935, is not a tax upon the airplanes or parts delivered under the contract, but is a tax with respect to individuals in the employment of the contractor. It is a payroll tax and not a tax upon the production, manufacture, or sale of the airplanes.

36 5. This question has been previously considered by the Comptroller General of the United States and his opinion A-84124 dated March 6, 1937, is in accord with the information herein contained.

6. Accordingly you are advised that any invoice predicated upon the claim disclosed by your letter will not receive favorable consideration. It, therefore, appears unnecessary to advise you further with respect to proper procedure involved in an appropriate case.

For the Chief of the Material Division:

W. F. VOLANDT,
Lt. Colonel, Air Corps,
Chief, Procurement Section.

37 *Exhibit C attached to amended petition of plaintiff*

In reply refer to EHS: bkh: 63.

OCTOBER 25, 1937.

Contract W 535 ac-650

The GLENN L. MARTIN COMPANY,
Baltimore, Maryland.

1. Your letter dated October 21, 1937, file 3227, in further reference to the matter raised in your letter of October 14, 1937, file 3212, to which answer was made in letter of this office addressed to you under date of October 18, 1937, has been received.

2. It is noted that you invite attention to the fact that the claim you have in mind is to be predicated upon Section 901, Title IX, of the Act of Congress approved August 14, 1935, Public No. 271, 74th Congress, in lieu of Section 804 thereof as previously supposed by this office. So much of Section 901 considered by you as applicable to your claim is as follows:

"On and after January 1, 1936, every employer (as defined in Section 907) shall pay for each calendar year an excise tax, with respect to having individuals in his employ, equal to the following percentages of the total wages (as defined in Section 907) payable

by him (regardless of the time of payment) with respect to employment (as defined in Section 907) during such calendar year:

"(1) With respect to employment during the calendar year 1936 the rate shall be 1 per centum; * * *"

Contract concluded in the fall of 1936.

3. It appears that Section 901 does have application with respect to individuals in your employment engaged upon subject contract in the year 1936, yet in the opinion of the Comptroller General
38 of the United States, A–84124, dated March 6, 1937, the tax imposed is not made applicable directly upon production, manufacture, or sale of the supplies called for under the terms of subject contract within the meaning of paragraph (3) of Article 17 thereof. It is, on the contrary, as heretofore advised, a pay-roll tax with respect to individuals in your employment at the time in question. Sections 804 and 901 are distinguishable only in the categories of employees to which they relate.

4. The information and advise heretofore conveyed to you in letter dated October 18, 1937, hereinabove referred to, is considered applicable to taxes imposed by Section 901 as well as Section 804 of the Social Security Act. A copy of the opinion of the Comptroller General of the United States, A–84124, is furnished herewith for your information and guidance.

For the Chief of the Material Division:

W. F. VOLANDT,
Lt. Colonel, Air Corps,
Chief, Procurement Section.

1 Incl.
Opinion of Comp. Gen. of U. S. No. A–84124 dated 3/6/37.

39 *Exhibit D attached to amended petition of plaintiff*

NOVEMBER 10, 1937.

From: The Glenn L. Martin Company, Baltimore, Maryland.
To: Finance Officer, Wright Field, Dayton, Ohio.
Thru: Representative, Air Corps, U. S. Army, Baltimore, Maryland
Subject: Claim for Refund of Social Security Tax—Forwarding o Invoice.
Reference: (a) Contract W 535ac-6861 dated June 28, 1934.
Enclosure: (A) 4 Copies GLM Invoice No. G-4108.

1. We are attaching hereto our Invoice No. G-4108 for $7,737.3 Enclosure (A), covering our claim for refund of Social Securit Taxes paid on total expenditures for labor during the years 1936 an 1937, on U. S. Army Contract No. W 535ac-6861, which was signe on June 28, 1934, which is prior to the effective date, i. e., August 1 1935, of the Social Security Act.

2. If the enclosed Invoice is not paid within thirty days, we wi assume that our claim is rejected; whereupon we will proceed to te the opinion of the Comptroller General of the United States N

A-84124 dated March 6, 1937, as we consider the Social Security Taxes applicable directly upon production, manufacture or sale of the supplies called for in the Contract, Reference (a), recoverable in full, as stipulated in Article 17, Paragraph 3, of the Contract.

Yours very truly,

THE GLENN L. MARTIN COMPANY,
By M. G. SHOOK, *Treasurer.*

MGS:P
c. c. W. Randall Compton of Semmes, Bowen & Semmes.

40 *Exhibit E attached to amended petition of plaintiff*

G-4108.

NOVEMBER 10, 1937.

W 535ac-6861 dated June 28, 1934. Net Cash.
FINANCE OFFICER, *Wright Field, Dayton, Ohio.*

Social Security Taxes paid on expenditures for Labor during the years 1936 and 1937, on U. S. Army Contract W 535-ac6861, signed on June 28, 1934, $7,737.32.

Total Claim in accordance with the following:

Year	Labor	Unemployment insurance tax	Old age benefit tax	Total claim
1936	$766,962.82	$7,669.63		$7,669.63
1937	2,256.48	45.13	$22.56	67.69
Totals	769,219.30	7,714.76	22.56	7,737.32

It is hereby certified that the above is correct and just, and that payment therefor has not been received.

THE GLENN L. MARTIN COMPANY,
By M. G. SHOOK, *Treasurer.*

41 *Exhibit F attached to amended petition of plaintiff*

HEADQUARTERS, WRIGHT FIELD,
OFFICE OF THE FINANCE OFFICER,
Dayton, Ohio, November 24, 1937.

Subject:
Social Security Taxes
Contract W 535 ac 6861
To: The Glenn L. Martin Company, Baltimore, Maryland.

1. Answering your letter of November 10, 1937 (MGS*P) to which you have attached Invoice G-4108 dated November 10, 1937, in amount of $7,737.32, covering claim for social security taxes paid during the years 1936 and 1937 on Contract W 535 ac 6861, be advised that this office is unable to pay this claim in view of Decision of the Comptroller General of the United States No. A-84124 dated March 6, 1937.

2. In view of the above, your invoice is returned for cancellation.

JOHN F. CONNELL,
Captain, F. D., Finance Officer.

42 [Clerk's Certificate to foregoing transcript omitted in printing.]

43 Same day, to wit, September 28, 1938, Plaintiff's Exhibit No. 1 is certified up.

In United States Circuit Court of Appeals

Minute entry of argument and submission

November 10, 1938, cause came on to be heard before Parker and Northcott, Circuit Judges, and H. H. Watkins, District Judge, and is argued by counsel and submitted.

44 In United States Circuit Court of Appeals, Fourth Circuit

No. 4375

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, APPELLANT

vs.

UNITED STATES OF AMERICA, APPELLEE

Appeal from the District Court of the United States for the District of Maryland, at Baltimore

(Argued November 10, 1938. Decided January 9, 1939)

Before PARKER and NORTHCOTT, Circuit Judges, and H. H. WATKINS, District Judge.

John T. Koehler (Semmes, Bowen & Semmes on brief) for Apellant, and James E. Murphy, Special Assistant to the Attorney General (James W. Morris, Assistant Attorney General; Sewall Key, Special Assistant to the Attorney General; Bernard J. Flynn, U. S. Attorney, and G. Randolph Aiken, Assistant U. S. Attorney, on brief) for Appellee.

Opinion

Filed January 9, 1939

PARKER, Circuit Judge:

This is an appeal by plaintiff from an adverse judgment in
45 a suit instituted under the Tucker Act to recover of the United States the sum of $7,737.32, alleged to be due under a government contract because of plaintiff's being required to pay social security taxes in that amount. Under the contract, which was executed June 25, 1934, prior to the passage of the Federal Social Security

Act of August 14, 1935, 49 Stat. 620, plaintiff agreed, for a stipulated price, to supply to the United States certain aircraft and aircraft materials. That contract contained the following provision:

"It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any federal tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture or sale of the supplies called for herein and are paid by the contractor on the articles or supplies herein contracted for, then the prices herein stipulated will be increased or decreased accordingly and any amount due the contractor as result of such change will be charged to the Government and entered on vouchers as separate items."

Something over a year after the execution of this contract Congress enacted the Federal Social Security Act, 49 Stat. 620, the following provisions of which are pertinent here:

"SEC. 804. In addition to other taxes, every employer shall pay an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages * * * paid by him after December 31, 1936, with respect to employment * * * after such date:

"(1) With respect to employment during the calendar years 1937, 1938, and 1939, the rate shall be 1 per centum."

"SEC. 901. On and after January 1, 1936, every employer 46 * * * shall pay for each calendar year an excise tax, with respect to having individuals in his employ, equal to the following percentages of the total wages * * * payable by him (regardless of the time of payment) with respect to employment * * * during such calendar year:

"(1) With respect to employment during the calendar year 1936 the rate shall be 1 per centum:

"(2) With respect to employment during the calendar year 1937 the rate shall be 2 per centum.

"SEC. 902. The taxpayer may credit against the tax imposed by section 901 the amount of contributions, with respect to employment during the taxable year, paid by him (before the date of filing his return for the taxable year) into an unemployment fund under a state law. The total credit allowed to a taxpayer under this section for all contributions paid into unemployment funds with respect to employment during such taxable year shall not exceed 90 per centum of the tax against which it is credited, and credit shall be allowed only for contributions made under the laws of states certified for the taxable year as provided in section 903."

Following the passage of the Social Security Act, plaintiff paid social security taxes in the amount of $7,737.32 for the years 1936 and 1937

on expenditures for labor employed in producing the supplies called for by the contract. Of this amount, $5,616.06 was paid as tax on sums paid to laborers engaged solely in the production or manufacture of these supplies. The remainder represents the portion of the tax paid on disbursements on account of "overhead" labor, and allocable to this contract, i. e., disbursements to employees who were engaged in production under other contracts as well as under the one here involved; and there is no contention that this allocation was not properly made in accordance with correct accounting principles. Of the total amount of the taxes paid, $6,943.29 was paid to the State of Maryland and credit on the federal tax was allowed therefor under section 902 of the Act quoted above.

47 The court below found for the government on the ground that the taxes paid by plaintiff were not "applicable *directly* upon production, manufacture, or sale" (23 F. Supp. 262, 264); and the plaintiff, having preserved its right of review by the presentation of appropriate prayers and exceptions duly entered, brings this appeal, contending that it is entitled, on the undisputed facts, to recover the amount sued for as a matter of law. The government contends that the judgment denying recovery should be affirmed, and that, in any event, plaintiff is entitled to recover no more than the amount of the taxes actually paid to the federal government, not including the part of the levies paid to the State of Maryland. Two questions, therefore, are presented for our consideration in interpretation of the contract sued on: (1) Whether the social security taxes imposed by the Act are "taxes or charges" made directly applicable upon production or manufacture; and (2) if so, whether that portion of the taxes paid to the State of Maryland and credited on the amount due under the federal Act are taxes "imposed by Congress" and "paid by the contractor" within the meaning of the contract. We think that both of these questions must be answered in the affirmative.

The taxes imposed by the Social Security Act are excise taxes and are so termed by the Act itself. They are imposed upon the relation of employment as one of the relationships embraced in the carrying on of business; and are sustained on the principle that "the power to tax the activities and relations that constitute a calling considered as a unit is the power to tax any of them. The whole includes the parts." Steward Machine Co. v. Davis, 301 U. S. 548, 581. Helvering v. Davis, 301 U. S. 619, 645. And because the tax is one upon the relation of employment, it is argued that it cannot be a tax "applicable directly" upon production or manufacture. We think, however, that, not this conclusion, but the contrary, is

48 the one which logically follows. As the whole is the sum of all its parts, a tax applicable directly on one of the parts is necessarily applicable directly on the whole which comprises it. The manufacture or production of the supplies called for by the contract necessarily involves the employment of labor and the use of mate-

rials; and a tax applicable directly upon either is a tax applicable directly upon the manufacture or production itself. No tax more directly applicable upon manufacture or production can be conceived, we think, than a pay-roll tax measured by wages paid to labor engaged therein.

It is argued that the contract should be interpreted as contemplating only taxes imposed by Congress on the production or manufacture of the particular articles called for by the contract and "measured by the number of units produced or sold or by weight or by some other unit of use or manufacture." We see no reason, however, to thus restrict the language used, which contains no provision that the tax imposed must be measured in any such way, but is of the broadest possible scope, including "any sales tax, processing tax, adjustment charge, or *other taxes or charges*." [Italics supplied.] The only limitation is that such taxes or charges be "applicable directly" upon production, manufacture, or sale; and, as we have seen, a tax "applicable directly" upon the employment of labor engaged in manufacture is "applicable directly" upon the manufacture or production in which that labor is engaged.

The language of the contractural provision is so clear, we think, as not to justify our looking beyond its plain meaning. If, however, we look to the purpose and intent of the parties, the provision was evidently inserted to protect the contractor against loss arising from the imposition of new or additional federal taxes, which would increase his cost of production but could not be anticipated with any degree of accuracy; and no tax could more clearly fall within the class of taxes which it was the purpose to provide against than
19 an employment tax measured by the wages paid to produce the articles which the contract called for. The taxes, it will be noted, are to be applicable directly upon the "manufacture, production, or sale" of the articles, not directly upon the articles themselves; and this requirement of directness is satisfied where the tax is imposed on some essential element of "manufacture, production, or sale" in such way as to constitute a direct burden upon same. It excludes, of course, such taxes as do not directly burden "manufacture, production, or sale," such as income, excess-profits, and capital-stock taxes.

The learned judge below was of opinion that the tax operated "indirectly through overhead expense rather than directly, as would increased wages paid for the work done." But a pay-roll tax measured by the wages paid to produce an article burdens production and increases the cost thereof to the same extent and in substantially the same way as increased wages. If the employer must pay three cents tax on every dollar paid in wages for the production of an article, the expense of producing the particular article is increased by just that much; and upon no possible theory can it be said that the tax is an investment of a permanent nature which would justify its being charged to overhead. And the settled accounting practice is that

such taxes should be charged to current expense and not to overhea
Cole, "Accounts; Their Construction and Interpretation," pp. 1
226, 227; Neuner, "Cost Accounting," p. 196; N. A. C. A. Bulleti
vol. XVIII, No. 24, Aug. 15, 1937, pp. 1376–1377.

Coming to the second question, i. e., whether the portion of t
tax paid to the State of Maryland and credited against the tax d
under the Act to the federal government falls within the meani
of the clause of the contract under consideration, it is to be not
that this portion, as well as the remainder, falls squarely within t
language used. The entire amount of the tax was "impose
50 by Congress and was "paid by the contractor." That a p
of it was paid with the consent of Congress to the State
Maryland and credited against the amount which would otherw
have been due under the Act, would seem to be immaterial. A ve
similar question was before the Court of Claims in *Batavia Mi
Inc.* v. *United States* (decided June 1, 1937, but unreported). The
a processing tax on cotton yarn had been paid by the manufactu
of cotton cloth to the seller of the yarn pursuant to the terms o
contract under which the yarn was purchased. The manufacturer
the cloth had sold it to the government under a contract providi
that the price should be increased by the amount of any new ta
made applicable by Congress to the supplies to be furnished after
date of the bid. In holding that the amount of the tax so p
might be recovered by the manufacturer of the cloth, who had
paid it to the government but to the processor of the yarn, the co
said:

"This is not a suit for the refund of taxes paid but an act
based upon the provisions of a contract. The provisions of the
with reference to refunds of taxes collected under the Agricultu
Adjustment Act have therefore no application. All of the matt
necessary to establish plaintiff's claim under the contract are sho
After the contract was entered into a new and additional tax
imposed on the manufacturer from whom the contract supplies w
purchased by plaintiff. The tax was passed on by the manufactu
and under the terms of plaintiff's contract with the manufactu
it was obliged to pay it. Defendant expressly agreed that the amo
of the tax should be added to the purchase price. The right
plaintiff to recover the amount so paid is clear and judgment
be rendered accordingly."

The Federal Social Security taxes were imposed by Congress
part of a comprehensive plan in which the states were expected
participate. That the states might be induced to do this, it was
vided in the Act that the taxpayer might credit against the
imposed by it any contributions paid by him into a state un
51 ployment fund, to an amount not exceeding 90% of the amo
of the tax under the federal Act. This, of course, was
more than permission to the taxpayer to pay to the state 90%
the tax imposed by the Act and to credit same as a deduction

the federal tax; and where the plaintiff availed itself of this privilege, paying a portion of the tax imposed to the state and claiming credit therefor under the Act, we think that it comes within the protection of the spirit as well as the language of the clause in the contract here under consideration. Even though the taxpayer was under legal obligation to pay the state tax to the state, the fact remains that that tax was imposed in connection with the general system brought into being by the federal Act and payment thereof was recognized as satisfying 90% of the obligation imposed by the federal tax. See Sections 903 and 904; Steward Mach. Co. v. Davis, 301 U. S. 548. If the state had not imposed a tax and established an unemployment fund complying with the requirements of the federal Act, the entire amount of the federal tax, without credit, would have been collected by the federal government and plaintiff would unquestionably have been entitled to recover same under the contract provision. We think it is in no worse plight because the state has seen fit to comply with the provisions of the federal Act and thus receive 90% of the tax that it imposes. The clause of the contract was intended to protect plaintiff against new taxes to be imposed by the federal government. It should not be denied this protection because that government permits a portion of the taxes imposed to be paid to the states under a general scheme for state and federal cooperation.

For the reason stated, the judgment appealed from will be reversed.

Reserved.

32 In United States Circuit Court of Appeals, Fourth Circuit

No. 4375

THE GLENN L. MARTIN COMPANY, A BODY CORPORATE, APPELLANT

vs.

UNITED STATES OF AMERICA, APPELLEE

Appeal from the District Court of the United States for the District of Maryland

Judgment

Filed and Entered January 9, 1939

This cause came on to be heard on the transcript of the record from the District Court of the United States for the District of Maryland, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court appealed from, in this cause, be, and the same is hereby, reversed; and that this cause be, and the same is hereby, remanded to the District Court of the United States for the District of Maryland, at Balti-

53 more, with directions to set aside the verdict and grant a new trial in accordance with the opinion of the Court filed herein.

January 9th, 1939.

JOHN J. PARKER,
Senior Circuit Judge.

Recital as to issuance of mandate

On another day, to wit, February 9, 1939, the mandate of this Court in this cause is issued and transmitted to the District Court of the United States for the District of Maryland, at Baltimore, in due form.

Same day, the original petition for appeal, order allowing appeal, and bond are returned to the Clerk of the District Court at Baltimore, Maryland.

Same day, the original exhibit (Plaintiff's Exhibit No. 1) is returned to the Clerk of the District Court at Baltimore, Maryland.

54 [Clerk's certificate to foregoing transcript omitted in printing.]

55 Supreme Court of the United States

Order allowing certiorari

Filed May 1, 1939

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Fourth Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Endorsement on cover:] Enter: Attorney General. File No. 43339. U. S. Circuit Court of Appeals, Fourth Circuit. Term No. 854. The United States of America, petitioner, vs. The Glenn L. Martin Company. Petition for writ of certiorari and exhibit thereto. Filed April 8, 1939. Term No. 854 O. T. 1938.

U. S. GOVERNMENT PRINTING OFFICE 1939